AUG 8 1940
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1940.

No. 316

JACOB MEHRLUST,

Petitioner,

—against—

JOSEPH T. HIGGINS, individually and as Collector of Internal Revenue for the Third District of New York,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT AND BRIEF IN SUPPORT THEREOF.

ANDREW B. TRUDGIAN,
Counsel for Petitioner.

DAVID J. LEVY,
Of Counsel.

August, 1940.

THE COURT PRESS, N. Y. C.

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JACOB MEHRLUST,

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—against—

JOSEPH T. HIGGINS, individually and as Collector of Internal Revenue for the Third District of New York,

Respondent.

Petition for Writ of Certiorari to the Circuit Court of Appeals for the Second Circuit.

Petitioner respectfully prays that a writ of certiorari issue to review a judgment of the Circuit Court of Appeals for the Second Circuit reversing a judgment of the District Court for the Southern District of New York in favor of the plaintiff in an action to recover a refund of Federal Manufacturers' Excise tax assessed under Section 605 of the Revenue Act of 1932.

OPINIONS BELOW.

The opinion of the District Court (R. 36) is reported in 30 F. Supp. 166. The opinion of the Circuit Court of Appeals (R. 47) has not yet been reported.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered on July 3, 1940 (R. 51). The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925.

Question Presented.

Whether petitioner was subject to manufacturer's excise tax, under Section 605 of the Revenue Act of 1932, on sales of jewelry after the effective date of the tax by a corporation of which he was the sole stockholder and to which he had sold such jewelry before such effective date?

Statutes and Regulations Involved.

The pertinent statutes and regulations involved are set forth in the Appendix, *infra*, pages 19 to 21.

Statement.

Section 605 of the Revenue Act of 1932, passed June 6, 1932, imposed an excise tax of 10% on sales of jewelry during the period June 21, 1932, to July 1, 1934, by a manufacturer, producer or importer. The law was not effective until fifteen days after its passage giving manufacturers an opportunity during this period of selling without tax as much of their manufactured stock as their selling facilities enabled them to dispose of. Under Section 619 of the Act, the tax was to apply to sales made after its effective date even though not arm's length transactions. There was no provision with respect to such transactions before such effective date.

Petitioner, a manufacturer of jewelry long prior to June 6, 1932, organized, on June 17, 1932, a corporation, J. Mehrlust, Inc., and in consideration of $2,500.00 in cash paid into its treasury, acquired 500 of its authorized 1,000 shares of no par value stock thus becoming its sole stockholder. On June 18th, he also sold to it, for $628,243.00, his stock of completely manufactured jewelry receiving the company's demand note for $626,243.00 and $2,000.00 in cash.

On June 18, 1932, the petitioner owed the banks some $235,000.00 in notes and had been repeatedly questioned by the banks as to the status of his affairs. The company paid in part its debt to him by giving to these banks its notes, endorsed by him, in exchange for his notes, the bank debts thus becoming funded and protected from the risks of his individual business. By January 1, 1939, the company's note to him had been reduced to $84,000.00, in part by it assuming his obligations to the banks and in part by other payments.

After the effective date of the Act, the company proceeded to sell to the general trade the manufactured jewelry it had so acquired, and petitioner continued to manufacture and sell to the general trade, as before, but made no further sales to the company. The company maintained its own separate books and records, and bank account, and filed its own separate tax returns to the Federal and State authorities.

Petitioner paid the excise tax on all sales of jewelry manufactured and sold by him individually after an effective date of the Act, but the corporation did not pay tax on its sales on the ground that it was not a manufacturer, producer or importer of the articles sold. The Commissioner, however, disregarded the sale of June 18, 1932, and taxed petitioner as though he had continued to sell the jewelry. Petitioner paid the taxes so levied

and was not reimbursed therefor. Thereafter he filed a claim for refund of the amount so paid and upon its rejection sued the Collector of Internal Revenue of the Third District of New York in the United States District Court, Southern District of New York. The case was tried to a judge upon an agreed state of facts, and judgment was entered for petitioner. The Circuit Court of Appeals has reversed this judgment.

Specification of Errors.

The Circuit Court of Appeals erred:

(1) In disregarding the intent of the Revenue Act of 1932 that no tax should apply on the articles of jewelry sold by petitioner to J. Mehrlust, Inc., before the effective date of the Act.

(2) In holding that the Treasury Department may, in all cases, if it sees fit, disregard a corporation for the purpose of taxing its stockholder.

(3) In disregarding the large outside interests in the corporation, represented by the banks, and considering it one which, because there was a single stockholder, might be disregarded by the Treasury Department.

Reasons for Granting the Writ.

1. The decision of the District Court was reversed because the Circuit Court of Appeals interpreted the income tax case of *Higgins* v. *Smith*, 308 U. S. 473, as establishing the rule that the Treasury Department may, in all cases, if it sees fit, disregard a corporation and tax its stockholder. It is the opinion of the Circuit Court

of Appeals that this rule applies regardless of the fact that the corporation has kept all necessary records and carried on its own business like any other merchant; and regardless of the fact that the corporate property is subject to its own creditors alone (R. 48, 49).

The District Court found that petitioner had divorced himself from all title to the merchandise (R. 40); that there had been a bona fide sale between two separate legal entities: the petitioner and the corporation (R. 40), and that the corporation exercised power and control over the merchandise transferred and was not a mere sales agency for the petitioner (R. 40). It also found, in connection with the fact that sales by petitioner before the effective date of the tax would escape the tax, that it was not compelled "to require an over-the-counter sale to defeat" the tax (R. 39). The Circuit Court of Appeals did not reverse the District Court on these findings but, as stated, on the basis of the general rule of law which it understood to have been established in *Higgins* v. *Smith*, *supra*.

It is submitted that a reading of the opinion of the court in *Higgins* v. *Smith*, *supra*, does not reveal that there is a general rule enunciated in that case, as found by the Circuit Court of Appeals, but that the Court merely referred to the right of the government to disregard a fiction. As a matter of fact, that case contains a warning against drawing conclusions as to the establishment of general rules in that when the government in that case urged that *Gregory* v. *Helvering*, 293 U. S. 465, was authority "for a realistic approach to tax situations" the Court retorted that "as so broad and unchallenged a principle furnishes only a general direction, it is of little value in the solution of tax problems".

If it is true that a general rule exists permitting the Treasury Department, as it sees fit, to ignore a jural

entity, the corporation, and reach the stockholder, it is important that the existence of that rule be more broadly enunciated. Moreover, the instant case is peculiarly adapted for such enunciation. Under Section 619 of the Revenue Act of 1932 there was to be the immediate recognition and taxation of sales between such interests as a stockholder and his company. This was because the tax under Section 605 was only to apply for a limited period and Congress wanted it to apply at once to such sales because, if it did not, the merchandise bought might not be resold before the tax went off and the government would lose revenue. Therefore, there could be no doubt as to the wide application of the rule if it were held in the instant case that the Treasury Department could ignore the sale by petitioner to the corporation before the effective date of the Act when, if such sale had occurred after such effective date, it would have been recognized and taxed.

2. It appears that there exists a conflict in the Circuit Courts of Appeal with reference to the principles enunciated in *Higgins* v. *Smith*, 303 U. S. 473, *supra*. In the instant case of *Mehrlust* v. *Higgins* the Circuit Court of Appeals for the Second Circuit regardless of the fact that the company was fully organized and doing business like any other merchant, and had property subject to its own creditors, alone, and without questioning the findings of the District Court as to the bona fides of the sale by the petitioner to the company, and the separateness of the stockholder and corporation, held that the stockholder was taxable under *Higgins* v. *Smith*, *supra*. On the other hand, as appears from the decision of the Circuit Court of Appeals of the Tenth Circuit in *Continental Oil Company* v. *Jones*, decided June 26, 1940, the United States Circuit Court of Appeals for the Tenth Circuit holds that whether

the separateness of corporate identity should be maintained or disregarded in a case involving tax problems depends upon the facts and circumstances in the particular case. There accordingly is a wide divergence between the views of these circuits and it is of the utmost importance that the true rule be made evident.

Conclusion.

For the foregoing reasons it is respectfully submitted that this petition for a writ of certiorari should be granted.

Respectfully submitted,

ANDREW B. TRUDGIAN,
Counsel for Petitioner.

David J. Levy,
Of Counsel.

August, 1940.

BRIEF IN SUPPORT OF THE PETITION.

Argument.

POINT I.

The Revenue Act of 1932 intended that no tax should be paid by appellee on the articles of jewelry sold by him to J. Mehrlust, Inc., before the effective date of the Act.

The tax imposed by Section 605 of the Revenue Act of 1932 applied only to sales by manufacturers, producers, and importers. Under the Act, there was a fifteen day interval from the time it became a law to its effective date within which manufacturers, producers, or importers of jewelry might dispose of articles already manufactured, produced, or imported by them free of excise tax liability. Thereafter when these same articles were sold no excise tax would be paid on such sales because they were not sales by the manufacturers, producers, or importers of such articles.

That the purpose of the fifteen day interval was to enable manufacturers, producers or importers to avoid the excise tax on the completed merchandise owned by them on June 6, 1932, is peculiary evident from the fact that the law did not provide for a floor tax. When the Agricultural Adjustment Act (Title 1, Public, No. 10, Seventy-third Congress) provided for a processing tax on certain articles thereafter to be processed, it likewise provided that such articles already processed should bear an equalizing tax called a floor tax. Likewise, when the Revenue Acts of 1918, 1934, and 1938, imposed increased taxes on the withdrawal of distilled spirits from bond, they imposed at the same time an equalizing floor tax on

distilled spirits already withdrawn. The purpose of floor taxes is to do equity between persons, and prevent them being placed in a position where they cannot equally compete with others in the same line of business. Excise taxes as heavy as the 10% tax imposed by Section 605 of the Revenue Act of 1932 of necessity add a most considerable burden to sales and unless some other relief is afforded, such as a tax operating only *in futuro*, a floor tax is necessary or a burden will fall more heavily on one competitor than another.

From the repeated imposition of floor taxes under various tax laws, it is most readily apparent that Congress recognizes the economic necessity for equality in competition and where necessary has attempted to bring this about. Therefore, when Congress failed to enact an equalizing floor tax in connection with the heavy tax imposed by Section 605, but instead provided a term of fifteen days before the effective date of the tax, thus enabling manufacturers, producers or importers to avoid such tax on their finished merchandise on hand by their sale, it is most apparent that they felt equalization was necessary and being accomplished by the fifteen day interval. As evidence that such was the intent and spirit of Congress, the following is quoted from the Report—Ways and Means Committee (72d Cong., 1st Sess., H. Rept. 708)—Title IV—Manufacturers' Excise Tax—Certainly as to Tax Liability:

> "Retroactive imposition of the tax, or change in the method by which the tax is computed, necessarily results in hardship and dissatisfaction, which in turn will bring about the break-down of the tax."

But equalization in the instant case could only be accomplished through the instrumentality of these fifteen

days if a sale before the effective date of the act to a wholly owned company could be recognized as an effective sale, so that no tax would be imposed on the seller when the articles sold were subsequently disposed of by the purchaser from him. Otherwise, the tax burden would fall most heavily on those who could least bear it. For a prosperous, well-organized company with an ultra-efficient sales organization could, within the fifteen days, escape tax by disposing of all its taxable articles to numerous customers. On the other hand, the struggling taxpayer who could not as well bear the burden of the tax because of his financial and business condition could not, because of his lack of a proper sales organization, dispose of taxable articles to the general market and thus avoid the tax as Congress intended. He could, however, readily dispose of such articles to a single customer, a wholly owned company not a manufacturer, producer or importer, and if such a sale is recognized, accomplish what Congress intended.

In this connection, it is pointed out that on June 6, 1932, there was finished jewelry for sale by retailers and wholesalers, and by manufacturers, producers, and importers. The jewelry being offered for sale by others than the manufacturers, producers, or importers could indisputably have been sold for a greater profit and yet for a less price than the articles then in the hands of the manufacturers, producers, or importers, if it were not for the fact that Congress granted fifteen days within which the manufacturer, producer or importer might sell his goods and place them on a price parity with wholesalers' and retailers' goods. The law did not limit the types of customers to whom the manufacturer, producer, or importer could sell. If, then, a manufacturer, producer, or importer sold to a single company, wholly owned by him, the goods he had on hand prior to the effective date of

the Act, he was merely accomplishing the intent of Congress and such sale should be recognized.

That it was the intent of Congress that a sale to a wholly owned company before the effective date of the Act should be recognized is further evidenced by the fact that there is no provision forbidding or covering such transactions, but with respect to such sale occurring after the effective date of the Act, Congress specifically provided in Section 619 (b) of the Revenue Act of 1932:

> "If an article is—
>
> (1) Sold at retail
>
> (2) sold on consignment; or
>
> (3) sold (otherwise than through an arm's-length transaction) at less than the fair market price; the tax under this title shall (if based on the price for which the article is sold) be computed on the price for which such articles are sold, in the ordinary course of trade, by manufacturers or producers thereof, as determined by the Commissioner."

Congress, as is evident from Section 619 (b), knew that sales would be made after the effective date of the Act to wholly owned companies. For purposes of the tax, Congress recognized such sales and provided for manufacturer's excise tax thereon. But it did not provide anything with respect to such sales occurring before the effective date of the Act, a most emphatic indication, especially when coupled with the future application of the law, that it intended that such sales might be made and tax avoided.

POINT II.

There is no general rule that the Treasury Department may in all cases, if it sees fit, disregard a corporation for the purpose of taxing its stockholder.

The Circuit Court of Appeals based its decision on *Higgins* v. *Smith*, 303 U. S. 473, *supra*. That case arose under the Revenue Act of 1932 and involved the right of a taxpayer to deduct, in determining his taxable income, a loss resulting from a sale of securities to a wholly owned company. The Court held that "the sale was ineffective to close a transaction for the determination of loss". The Court stated:

> "There is not enough of substance in such a sale finally to determine a loss."

But, *Higgins* v. *Smith*, *supra*, established no universal rule and certainly does not apply in the instant case. The income tax law contained no Section 619 (b) wherein Congress recognized the validity of sales between related identities and provided specifically with reference to the applicable tax base in the case of such sales to prevent tax avoidance. In this connection the following is quoted from the Report—Ways and Means Committee (72d Cong., 1st Sess., H. Rept. 708):

> "Third, provision is made for transactions in which, by reason of the relationship of the parties, the price charged does not represent a fair value arrived at by an arm's-length sale. For example, a manufacturer may transfer his product to a selling agency controlled by him, at a book-keeping price below market value. Or a manufacturing corporation may sell plant equipment to an affiliated concern at an arbitrary price. It is essential that in

such cases the tax be imposed on the same value as in the case of similar sales between independent parties."

In this connection also the following is quoted from a published ruling of the Treasury Department itself:

> "Section 619 (b) 3 is undoubtedly intended to prevent the avoidance of taxes which would easily be possible without its presence in the law. Congress apparently foresaw the probability of the creation of corporations having identical interests, one as the manufacturer and the other as the distributing agency, and sought to impose the tax on the full manufacturer's sales price where the manufacturing corporation sold to the distributing corporation at a nominal price. There are numerous other instances where similar mutual interests could operate to the disadvantage of the Government. Viewing the statute in this light, it must be presumed that Congress did not intend to have two or more affiliated corporations recognized as a single entity for manufacturers' excise tax purposes. If it had so intended it seems reasonable to believe that some provision would have been made in the statute for such recognition. That no such provision was made, coupled with the fact that transactions not at arm's-length are specifically provided for, leads to the conclusion that the intent was to impose a tax on all sales between such corporations." S. T. 617, XI-1 Cum. Bull. 513 (1932).

To repeat what was stated under Point I, Congress was fully alive to possible methods of escaping the excise tax by means of related taxpayers, and, nevertheless, recognized the validity of transactions between them. It chose to provide a means of preventing tax avoidance in the case of sales between related persons

after the effective date of the Act, but not on sales prior thereto. In view of a specific provision after the effective date and none before, coupled with the future application of the law and the equity behind such future application, it is most apparent that Congress did not intend the tax to apply under the facts in the present case.

This is peculiarly clear when it is considered that to sustain the Government's position it must be held that there was no valid sale by J. Mehrlust to J. Mehrlust, Inc., when, if the identical transaction had happened after the effective date of the law, by specific provision of the law (Sec. 619(b)) such a sale would be recognized and taxed. Surely if a sale were valid under the law if made after a specific date, the same sale was valid within the intent of the law when made before that date. Congress could never have intended that the whole nature of an act is different merely because it occurred before or after a point of time.

While is is true that the Court in *Higgins* v. *Smith* used language that considered alone might be construed to have wide application—

> "On the other hand, the Government may not be required to acquiesce in the taxpayer's election of that form for doing business which is most advantageous to him. The Government may look at actualities and upon determination that the form for doing business or carrying out the challenged tax event is unreal or a sham may sustain or disregard the effect of the fiction as best serves the purpose of the tax statute."

—yet such language was used by the Court in connection with a specific state of facts before it and should be considered in the light of those peculiar facts. As a

caution against construing the language of a decision too broadly, reference is made to the case of *Koshland* v. *Helvering,* 298 U. S. 441, where the Court said:

> "Although *Eisner* v. *Macomber* affected only the taxation of dividends declared in the same stock as that presently held by the taxpayer, the Treasury gave the decision a broader interpretation which Congress followed in the Act of 1921."

Moreover, in *Higgins* v. *Smith, supra,* when the Government contended for a certain application of *Gregory* v. *Helvering,* 293 U. S. 465, the Supreme Court said:

> "The Government urges that the principle underlying *Gregory* v. *Helvering* finds expression in the rule calling for a realistic approach to tax situations. As so broad and unchallenged a principle furnishes only a general direction, it is of little value in the solution of tax problems."

POINT III.

Because of the outside interests in J. Mehrlust, Inc., represented by the banks, the corporation was not one which the Treasury Department might disregard as it saw fit.

At the time of the formation of J. Mehrlust, Inc., petitioner owed the banks on his notes the large sum of $235,000. So far as the banks were concerned, their obligations were on a parity with all other liabilities of the appellee, and subject to all the risks of additional liabilities to which the individual might subject himself, and it was necessary that they keep themselves constantly advised as to his affairs, especially during the trying and uncertain times of 1931 and early 1932.

Therefore, from time to time, the banks questioned him as to the status of his affairs. However, by the formation of J. Mehrlust, Inc., and that company becoming primarily liable to the banks, the bank indebtedness was protected by the assets of the corporation and was relieved from the danger of present and future risks of individual liabilities. Following its incorporation, J. Mehrlust, Inc., was not in reality a corporation wholly owned by appellee, but a corporation in which there was a large outside participation, the participation of the banks, who had a first claim on its assets and whose rights could not be lawfully invaded or jeopardized by the appellee. As a consequence J. Mehrlust, Inc., was not one that could be disregarded because of its identity with its stockholder.

CONCLUSION.

In view of the wide spread effect of the principles involved and to resolve the doubts as to the correctness of the decision below, it is respectfully submitted that the writ of certiorari should be granted.

Respectfully submitted,

ANDREW B. TRUDGIAN,
Counsel for Petitioner.

DAVID J. LEVY,
Of Counsel.

August, 1940.

APPENDIX.

Statutes and Regulations.

Sec. 605 of the Revenue Act of 1932.

"There is hereby imposed upon the following articles, sold by the manufacturer, producer, or importer, a tax equivalent to 10 per centum of the price for which so sold: All articles commonly or commercially known as jewelry, whether real or imitation; pearls, precious and semi-precious stones, and imitations thereof; articles made of, or ornamented, mounted or fitted with, precious metals or imitations thereof or ivory (not including surgical instruments or silver-plated ware, or frames or mountings for spectacles or eyeglasses); watches, clocks; parts for watches or clocks sold for more than 9 cents each; opera glasses; lorgnettes; marine glasses; field glasses; and binoculars. No tax shall be imposed under this section on any article used for religious purposes, or any article (other than watch parts or clock parts) sold for less than $3."

Sec. 619 of the Revenue Act of 1932.

"* * * (b) If an article is—

(1) sold at retail;

(2) sold on consignment; or

(3) sold (otherwise than through an arm's length transaction) at less than the fair market price;

the tax under this title shall (if based on the price for which the article is sold) be computed on the price for which such articles are sold, in the ordinary course of trade, by manufacturers or producers thereof, as determined by the Commissioner. * * *"

Sec. 623 of the Revenue Act of 1932.

"In case any person acquired from the manufacturer, producer, or importer of an article, by operation of law or as a result of any transaction not taxable under this title, the right to sell such article, the sale of such article by such person shall be taxable under this title as if made by the manufacturer, producer, or importer, and such person shall be liable for the tax."

Sec. 629 of the Revenue Act of 1932.

"This title shall take effect on the 15th day after the date of the enactment of this Act, except that section 628, relating to rules and regulations, and this section, shall take effect on the date of the enactment of this Act. No sale or importation after June 30, 1934 * * * shall be taxable under this title."

Sec. 212 of the National Industrial Recovery Act of 1933.

"Titles IV and V of the Revenue Act of 1932 are amended by striking out '1934' wherever appearing therein and by inserting in lieu thereof '1935'."

Sec. 609 of the Revenue Act of 1934.

"The tax imposed by section 605 of the Revenue Act of 1932 shall not apply to articles sold by the manufacturer, producer, or importer, after the date of the enactment of this Act, for less than $25."

Joint Resolution of June 28, 1935.

"* * * That title IV, as amended, and parts I, II, III and IV of title V, as amended, of the Revenue Act of 1932, are further amended by striking out '1935' wherever appearing therein, and inserting in lieu thereof '1937'. * * *"

Sec. 809 of the Revenue Act of 1936.

"The tax imposed by section 605 of the Revenue Act of 1932 shall not apply to any article sold by the manufacturer, producer, or importer after the date of the enactment of this Act."

Regulations 46, Relating to Excise Taxes on Sales by the Manufacturer under Sections 602 to 611, inclusive, 613, and 614 of the Revenue Act of 1932.

Art. 1. "The tax imposed under Title IV of the Revenue Act of 1932, is on articles sold, leased, or used by the manufacturer, producer, or importer on or after June 21, 1932, even though manufactured, produced, or imported before that date. * * *"

Art. 3. "The tax covered by these regulations shall be paid by the manufacturer, producer, or importer on all sales, whether made directly or through an agent, * * *."

Art. 4. "As used in the Act, the term 'producer' includes a person who produces a taxable article by processing, manipulating, or changing the form of an article, or produces a taxable article by combining or assembling two or more articles. * * *"

Art. 5. "In general the tax attaches when the title to the article sold passes from the manufacturer to a purchaser.

"When title passes is dependent upon the intention of the parties as gathered from the contract of sale and the attendant circumstances. In the absence of expressed intention, the legal rules of presumption followed in the jurisdiction where the sale is made govern in determining when title passes. Generally, title passes upon delivery of the articles to the purchaser or to a carrier for the purchaser.

"In the case of a sale on credit, it is immaterial whether or not the purchase price is actually collected."

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257329—40

In the Supreme Court of the United States

OCTOBER TERM, 1940

No. 316

JACOB MEHRLUST, PETITIONER

v.

JOSEPH T. HIGGINS, INDIVIDUALLY AND AS COLLECTOR OF INTERNAL REVENUE FOR THE THIRD DISTRICT OF NEW YORK

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINION BELOW

The opinion of the District Court (R. 36–41) is reported in 30 F. Supp. 166. The opinion of the Circuit Court of Appeals (R. 47–49) is reported in 112 F. (2d) 717.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on July 3, 1940. (R. 50–51.) The petition for a writ of certiorari was filed on August 8, 1940. The jurisdiction of this Court is invoked

under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the taxpayer's transfer of his stock of jewelry to a newly formed, wholly owned corporation three days before the effective date of Section 605 of the Revenue Act of 1932 was effective to avoid the manufacturer's excise taxes assessed against the taxpayer under that section upon the subsequent sales of the jewelry.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in the Appendix, *infra,* pp. 7–8.

STATEMENT

The material facts as stipulated (R. 27–34) and as found by the District Court (R. 37–39, 41) are as follows:

Section 605 of the Revenue Act of 1932 was enacted into law on June 6, 1932 and became effective on June 21 of that year. It imposed an excise tax of ten percent on sales of jewelry by a manufacturer, producer or importer.

Taxpayer, Jacob Mehrlust, who was engaged in the manufacture and sale of jewelry, had on hand on June 6, 1932 a stock of jewelry valued at $628,243. He organized a corporation, known as J. Mehrlust, Inc., on June 17, for 500 of whose 1,000 authorized shares of stock he paid into its

treasury $2,500 in cash. He thus became, and has since remained, the sole stockholder of the corporation and its only salaried officer. On June 18, the taxpayer sold to the corporation the stock of jewelry which he had on hand and took in exchange the company's demand note for $626,243, bearing no interest, and $2,000 in cash out of the $2,500 he had just paid in. The corporation paid the note in part by assuming a debt of the taxpayer in the amount of $235,000, which was owing to various banks. The corporation gave its notes, endorsed by the taxpayer, to the banks in place of the taxpayer's individual notes. (R. 37.)

After the transfer of the jewelry to the corporation, and after the effective date of Section 605, the corporation began to sell the jewelry as the taxpayer had done before. The clerical force and office space which it used were substantially the same as those previously used by the taxpayer as an individual. The corporation made no further purchases from the taxpayer, although it did make several purchases from others. The articles which it sold were invoiced under the corporate name on forms previously used by the individual, but to which was added a stamped "Inc.", which, in a few instances, was inadvertently omitted. Some checks came in payable to the corporation and some to the individual. Of the latter, some were endorsed by the individual and deposited in the corporate account and others were sent back to the customers to be redrawn. (R. 37–38.)

Some articles which were unsaleable were transferred back to the individual, who refabricated and sold them. Such retransfers were recorded in the stock book of the corporation with the notation "J. M.", sometimes accompanied by the legend "sold to" and at other times by the legend "charged to," but no entries were made in the corporation's sales book or the individual's purchase book and they were entered in the individual's journal under the designation "intercompany account". (R. 38.)

The corporation kept a complete set of books, maintained a separate bank account and filed separate tax returns. The taxpayer paid the operating expenses of the corporation in the first instance, but was then recompensed by the company. The corporation never had a telephone listing or a listing in the directory located in the lobby of the building in which it was situated. (R. 38–39.)

The Commissioner determined that the alleged sale from the taxpayer to the corporation "was not a bona fide transaction, but merely a scheme to escape tax liability" (R. 17), and accordingly ruled that the taxpayer was liable for a tax under Section 605 with respect to all sales by the corporation of jewelry acquired from the taxpayer. The taxpayer paid the tax under protest, filed a claim for refund which was rejected, and then instituted suit (R. 39). The District Court, holding that the sale from the taxpayer to the corporation was bona

fide, entered judgment for the respondent (R. 42–43). The court below reversed (R. 50).

ARGUMENT

The decision below is not in conflict with the decision of any other circuit court of appeals or with any decision of this Court and presents no question of importance. The issue is merely whether the rule of *Higgins* v. *Smith,* 308 U. S. 473, and *Griffiths* v. *Commissioner,* 308 U. S. 355, is applicable to the particular facts of this case; the decision of the court below that the rule does apply was plainly correct and, in any event, presents no occasion for further review.

There can be no dispute that, as the court below held, the corporation was "absolutely and immediately responsible" to the will of the taxpayer. Consequently, even though the corporation be deemed a separate legal entity which had legal title to the jewelry, its sales were, in every real sense, the sales of the taxpayer. The tax imposed by Section 605 is laid upon an act, the sale by a manufacturer; as the court below pointed out, the taxpayer could, and did, perform that act as much by means of his wholly owned and controlled corporation as though he had sold in his own name or in that of any other agent.

Petitioner alleges (Pet. 6–7) a conflict between the decision below and the decision of the Circuit Court of Appeals for the Tenth Circuit in *Continental Oil Co.* v. *Jones,* decided June 26, 1940, not

yet officially reported but found in 1940 C. C. H., Vol. 4, par. 9549. Far from being in conflict, the decisions are strikingly similar. There the taxpayer, which was a producer and manufacturer of lubricating oil, sought to avoid the impact of Section 601 (c) of the Revenue Act of 1932, which imposed an excise tax upon lubricating oil sold by a manufacturer or producer, by selling its lubricating oil prior to the effective date of Section 601 (c) to wholly owned and controlled corporations which were not producers or manufacturers. The court held, as the court below held in the present case, that under the decisions in *Higgins* v. *Smith, supra,* and *Griffiths* v. *Commissioner, supra,* the taxpayer was liable for the tax on subsequent sales of the oil made by the wholly owned corporations.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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SEPTEMBER, 1940.

APPENDIX

Revenue Act of 1932, c. 209, 47 Stat. 169:

SEC. 605. TAX ON JEWELRY, ETC.

There is hereby imposed upon the following articles, sold by the manufacturer, producer, or importer, a tax equivalent to 10 per centum of the price for which so sold: All articles commonly or commercially known as jewelry, whether real or imitation; pearls, precious and semiprecious stones, and imitations thereof; articles made of, or ornamented, mounted or fitted with, precious metals or imitations thereof or ivory (not including surgical instruments or silver-plated ware, or frames or mountings for spectacles or eyeglasses); watches; clocks; parts for watches or clocks sold for more than 9 cents each; opera glasses; lorgnettes; marine glasses; field glasses; and binoculars. No tax shall be imposed under this section on any article used for religious purposes, or any article (other than watch parts or clock parts) sold for less than $3.

* * * * *

SEC. 619. SALE PRICE.

* * * * *

(b) If an article is—

(1) sold at retail;

(2) sold on consignment; or

(3) sold (otherwise than through an arm's-length transaction) at less than the fair market price; the tax under this title shall (if based on the price for which the article is sold) be computed on the price for which such articles are sold, in the ordinary course of trade, by manufacturers or pro-

ducers thereof, as determined by the Commissioner.

* * * * *

SEC. 623. SALES BY OTHERS THAN MANUFACTURER, PRODUCER, OF IMPORTER.

In case any person acquires from the manufacturer, producer, or importer of an article, by operation of law or as a result of any transaction not taxable under this title, the right to sell such article, the sale of such article by such person shall be taxable under this title as if made by the manufacturer, producer, or importer, and such person shall be liable for the tax.

* * * * *

SEC. 629. EFFECTIVE DATE.

This title shall take effect on the fifteenth day after the date of the enactment of this Act * * *.

* * * * *

Treasury Regulations 46, promulgated under the Revenue Act of 1932:

ART. 3. *Liability of manufacturer for tax.*—The tax covered by these regulations shall be paid by the manufacturer, producer, or importer on all sales, whether made directly or through an agent, * * *.

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